Citi Research
Equities

17 December 2013 | 32 pages

Beverages
Western Europe | United Kingdom

Britvic (BVIC.L)

Fruit -Shooting the Lights Out?

- Target Price Change

- **A lot more to go for** — The stock has seen a strong performance in 2013 (+66% YTD), but we think there is more upside. We forecast 13% EPS CAGR for the next 3 years, which is almost best in class in our European staples coverage universe, and we believe there is a very good chance of upgrades, particularly from three sources: (1) Fruit Shoot intl, (2) further cost savings and (3) improving UK macro. In total, we believe the upside to our EPS forecasts could be 9-39% on a 4-5 year view, depending on the scenarios.
- **Fruit Shoot international could add up to £38m to our EBIT forecasts** — In the US it is just a question of time, we believe, before Fruit Shoot goes national and into multi-pack, which would open up a $2bn market. 10% share of that is worth £19m to EBIT, we estimate. And this assumes no growth in the market, which seems conservative given per cap kids' juice consumption is 1/3 of the UK level.
- **We believe the current cost savings plan is conservative** — Our benchmarking analysis suggests that Britvic could lift its margins to around 14% in the medium term, primarily by reducing SG&A. We believe this could add up to £20m to EBIT.
- **Improving UK macro could benefit too** — Citi economists expect UK household available cash in 2014-15 to grow at the fastest pace in 10 years (ex 2010). While there is no evidence yet, we believe this could drive a slight improvement in volumes and better channel mix, resulting in up to £9m EBIT uplift on a 2 year view.
- **Valuation does not look stretched** – While the 12-month forward PE (15.6x) looks high relative to its history, (1) Britvic is still the cheapest EU staple on PEG (1.39), on our estimates (2) the PEG discount vs the beverage sector is wider than the 5-year average and (3) Britvic's 10% premium to the FTSE-250, does not look demanding given the outlook.
- **Buy, 850p target (raised from 640p) –** Depending on how much of this upside comes through, we think CY17 EPS could be between 57p (our existing forecasts) and 78p (in a "positive" but, we think, realistic scenario). Under these different scenarios, we value the stock between 613-1,097p. Our new 850p TP incorporates for the first time the potential upside to earnings and is set on a scenario probability weighted basis.

Buy	1
Price (16 Dec 13)	£6.72
Target price	£8.50
from £6.40	
Expected share price return	26.6%
Expected dividend yield	2.8%
Expected total return	29.4%
Market Cap	£1,652M
	US$2,692M

Price Performance
(RIC: BVIC.L, BB: BVIC LN)

Britvic (GBP)

Year to 30 Sep	2012A	2013A	2014E	2015E	2016E
Sales (£M)	1,256.4	1,321.9	1,354.6	1,402.9	1,450.4
Profit Before Tax (£M)	84.4	108.1	131.5	148.7	164.6
Diluted EPS (p)	26.5	35.0	41.8	47.2	52.2
Diluted EPS (Old) (p)	26.5	35.0	41.8	47.2	52.2
PE (x)	25.3	19.2	16.1	14.2	12.9
EV/EBITDA (x)	14.0	12.0	10.6	9.7	8.8
DPS (p)	17.7	18.4	20.4	23.1	25.6
Net Div Yield (%)	2.6	2.7	3.0	3.4	3.8

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See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

BVIC.L: Fiscal year end 30-Sep — Price: £6.72; TP: £8.50; Market Cap: £1,653m; Recomm: Buy

Profit & Loss (£m)	2012	2013	2014E	2015E	2016E
Sales revenue	1,256	1,322	1,355	1,403	1,450
Cost of sales	-625	-647	-663	-687	-710
Gross profit	632	675	692	716	741
Gross Margin (%)	50.3	51.1	51.1	51.1	51.1
EBITDA (Adj)	157	179	201	218	233
EBITDA Margin (Adj) (%)	12.5	13.5	14.9	15.5	16.1
Depreciation	-34	-37	-38	-40	-42
Amortisation	-10	-7	-7	-7	-7
EBIT (Adj)	113	135	156	171	184
EBIT Margin (Adj) (%)	9.0	10.2	11.5	12.2	12.7
Net interest	-28	-27	-25	-22	-20
Associates	0	0	0	0	0
Non-op/Except	-7	-26	-30	-20	0
Pre-tax profit	78	83	102	129	165
Tax	-20	-21	-24	-30	-38
Extraord./Min.Int./Pref.div.	0	0	0	0	0
Reported net profit	57	62	77	98	127
Net Margin (%)	4.6	4.7	5.7	7.0	8.7
Core NPAT	66	86	103	117	130

Per share data	2012	2013	2014E	2015E	2016E
Reported EPS (p)	23.1	25.3	31.3	39.7	50.9
Core EPS (p)	26.5	35.0	41.8	47.2	52.2
DPS (p)	17.7	18.4	20.4	23.1	25.6
CFPS (p)	41.7	47.1	50.8	64.8	69.0
FCFPS (p)	24.0	36.3	23.7	45.9	48.9
BVPS (p)	15.3	16.7	29.1	47.8	75.0
Wtd avg ord shares (m)	242	243	245	246	247
Wtd avg diluted shares (m)	249	245	247	248	249

Growth rates	2012	2013	2014E	2015E	2016E
Sales revenue (%)	-2.6	5.2	2.5	3.6	3.4
EBIT (Adj) (%)	-16.5	19.8	15.8	9.3	7.8
Core NPAT (%)	-18.5	29.8	20.3	13.4	11.1
Core EPS (%)	-19.3	32.0	19.2	12.9	10.7

Balance Sheet (£m)	2012	2013	2014E	2015E	2016E
Cash & cash equiv.	50	94	77	97	96
Accounts receivables	261	270	275	283	292
Inventory	74	91	87	88	90
Net fixed & other tangibles	237	216	245	252	260
Goodwill & intangibles	305	317	318	316	314
Financial & other assets	92	75	1	1	11
Total assets	1,018	1,063	1,003	1,037	1,062
Accounts payable	357	382	393	408	424
Short-term debt	3	94	0	0	0
Long-term debt	559	458	448	418	368
Provisions & other liab	63	88	90	93	84
Total liabilities	981	1,022	931	919	876
Shareholders' equity	37	41	72	118	186
Minority interests	0	0	0	0	0
Total equity	37	41	72	118	186
Net debt	512	458	371	322	272
Net debt to equity (%)	nm	nm	518.3	272.6	146.3

Valuation ratios	2012	2013	2014E	2015E	2016E
PE (x)	25.3	19.2	16.1	14.2	12.9
PB (x)	43.8	40.2	23.1	14.1	9.0
EV/EBITDA (x)	14.0	12.0	10.6	9.7	8.8
FCF yield (%)	3.6	5.4	3.5	6.8	7.3
Dividend yield (%)	2.6	2.7	3.0	3.4	3.8
Payout ratio (%)	67	53	49	49	49
ROE (%)	192.6	158.7	137.2	103.9	83.4

Cashflow (£m)	2012	2013	2014E	2015E	2016E
EBITDA	157	179	201	218	233
Working capital	6	-10	2	6	6
Other	-59	-54	-78	-63	-68
Operating cashflow	104	115	125	161	172
Capex	-44	-26	-67	-47	-50
Net acq/disposals	2	0	0	0	0
Other	-5	-9	-8	-5	-5
Investing cashflow	-47	-35	-75	-52	-55
Dividends paid	-43	-43	-47	-52	-59
Financing cashflow	-51	-36	-65	-89	-117
Net change in cash	6	44	-14	19	0
Free cashflow to s/holders	60	89	58	114	122

Sales by Division (£ m)	2012	2013	2014E	2015E	2016E
GB Stills	322	340	347	359	370
GB Carbs	518	536	553	572	591
International	29	38	45	51	58
Ireland	139	137	135	138	141
France	249	271	275	283	290
Sales - total segments	1,256	1,322	1,355	1,403	1,450

Brand Contribution (£ m)	2012	2013	2014E	2015E	2016E
GB Stills	141	155	160	167	173
GB Carbs	189	200	210	219	227
International	8	14	16	17	20
Ireland	45	49	50	52	54
France	59	68	69	72	74
Total Brand Contribution	442	486	505	526	549

Brand Contri. Margin (%)	2012	2013	2014E	2015E	2016E
GB Stills	43.9	45.4	46.1	46.4	46.8
GB Carbs	36.4	37.3	37.9	38.2	38.5
International	28.3	37.6	35.6	33.6	34.6
Ireland	32.2	35.8	36.7	37.4	38.1
France	23.8	25.1	25.2	25.5	25.6
Group	35.2	36.7	37.3	37.5	37.8

For definitions of the items in this table, please click here.

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Investment Summary

We are reiterating our Buy recommendation on Britvic and raising our target price to 850p from 640p.

The shares have had a very good run, but we believe there is a lot more to come. We consider the growth in our existing forecasts to be compelling but, in our view, there is a good chance of significant upgrades from a variety of sources, and so the point of this note is to quantify and value the possible upside.

- **Existing Forecasts: Strong EPS growth outlook** – On our forecasts (which are broadly consensual[1]), Britvic delivers 13% EPS CAGR CY13-16E, almost best in class in our European staples coverage universe (Figure 9). We believe this growth outlook is both visible (it is underpinned by cost savings and recovery from the Fruit Shoot recall hit) and conservative (it implies 5% underlying EBIT growth per annum).

- **Areas that could drive material upgrades–** We see scope for material earnings upgrades over time, coming from 3 areas:

  1) **Fruit Shoot international** – The US roll-out is progressing very well: in some regions Fruit Shoot has achieved 20-25% market share, Pepsi has committed to a 15-year agreement and we believe it is just a question of time before Fruit Shoot goes national and into multi-pack, which would open up a $2bn market. If Fruit Shoot were to achieve just 10% share of that, we estimate this would be worth nearly £20m to EBIT (of which over half is incremental to our existing forecasts) and this assumes no growth in the market, which is probably unrealistic, as per cap kids' juice consumption in the US is only 1/3 of the UK level. Besides the US, Fruit Shoot is making good progress in France and the early signs in Spain, where it has just been launched, are positive too. In total, **we believe that, on realistic assumptions, international could add up to £38m to our existing FY17 EBIT forecast**. We address the international opportunity in detail on pages 10-16.

  2) **Further cost savings –**The current cost cutting plan is conservative in our view. Our benchmarking analysis suggests that Britvic could lift its margins to around 14% in the medium term, primarily by reducing SG&A which look high relative to peers. **Further cost cutting could add up to £20m to EBIT, in the medium term**. More detail on pages 16-17.

  3) **UK macro** – Citi economists expect a material acceleration in UK GDP growth in 2014 and 2015 and household available cash is expected to grow at the fastest pace in 10 years (ex 2010). This could drive slightly better volume growth and positive channel mix, with faster growth in the higher margin impulse and pubs & clubs channels. While there is no sign of improvement yet, we believe **the upside on a two year view could be up to £9m**. We discuss the implications of the macro and favourable input cost environment starting on page 18.

[1] We are 2% ahead of consensus on FY14 EPS (and at the top of the £148-156m guidance range on EBIT) and in line with consensus on FY15 EPS.

In total, we believe the upside to our existing forecasts could be very substantial indeed, up to almost 40% on a 4-5 year view, maybe more or maybe less. The exact quantum of the upside is difficult to determine, particularly the portion coming from international. We have therefore constructed **3 scenarios**:

- **Scenario A** is **Conservative**, we believe, because it assumes no benefit from the improving UK macro, no cost savings beyond the existing plan and a fairly cautious view on Fruit Shoot in the US.

- **Scenario B (Medium)** and **Scenario C (Positive)** are a bit more optimistic, but still realistic, in our opinion.

Figure 1. Britvic Scenario Analysis – Potential upside to Citi forecasts from UK macro, cost savings and Fruit Shoot international

		Scenario A CONSERVATIVE		Scenario B MEDIUM		Scenario C POSITIVE	
		EBIT (£ mln)	EPS (p)	EBIT (£ mln)	EPS (p)	EBIT (£ mln)	EPS (p)
	Citi Existing FY17 forecasts	193	56.1	193	56.1	193	56.1
Potential upside from	1. Fruit Shoot international (incremental to existing Citi estimates)	15	5.1	30	10.2	38	13.0
	2. Further cost savings	0	0	10	3.1	20	6.2
	3. Improving UK macro	0	0	4.5	1.4	9	2.8
	Total upside	15	5.1	45	14.7	67	22.0
	FY17 forecasts including potential earnings upside	208	61.2	238	70.8	260	78.1
	Accretion to Citi Existing FY17 forecasts	8%	9%	23%	26%	35%	39%

Note: the upside is calculated on FY17 estimates. We believe UK macro and cost savings benefits could be more front end loaded, but the timeframe from international is more difficult to determine. Source: Citi Research estimates

Figure 1 details the potential upside to our existing EBIT and EPS forecasts for each scenario and the following table shows the main assumptions that underpin them.

ASSUMPTIONS for:	Scenario A Conservative	Scenario B Medium	Scenario C Positive
UK Macro	■ No benefit	■ 0.25% extra vol growth in GB ■ 0.25% extra mix in GB	■ 0.5% extra vol growth in GB ■ 0.5% extra mix in GB
Further Cost Savings	■ No benefit	■ 80bps margin benefit in addition to current cost savings	■ 160bps margin benefit in addition to current cost savings
Fruit Shoot International	■ 10% share of US mkt ■ 15% share France, 10% Spain ■ No growth in US, France, Spain kids' juice mkt ■ Zero profit from new mkt entries	■ 12.5% share of US mkt ■ 20% share France, 20% Spain ■ 3% growth p.a. in US, France, Spain kids' juice mkt ■ £2m profit from new mkt entries	■ 15% share of US mkt ■ 20% share France, 20% Spain ■ 5-6% growth p.a. in US, France, Spain kids' juice mkt ■ £2m profit from new mkt entries

Valuation

On 15.6x CY14E PE (this is CY14, front page shows FY14), the shares do not look cheap relative to history (Figure 2), but we suggest a one-year forward multiple does not capture Britvic's good 3-year EPS growth outlook, nor the potential for material upgrades. We believe it is more meaningful to focus on the following metrics:

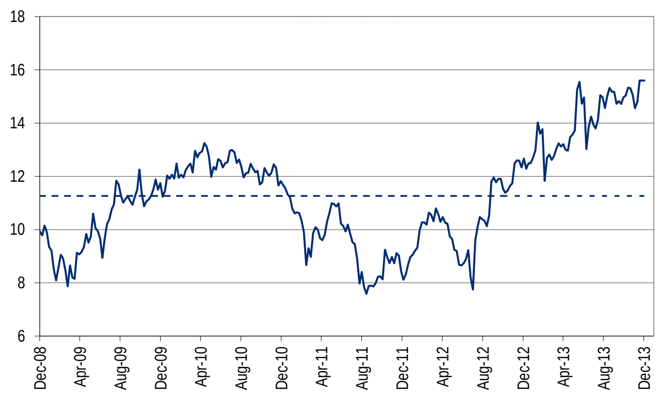
- **PE Relative** – Britvic trades at a 10% premium to the FTSE 250, which we don't think is demanding, given its growth outlook (Figure 3).

- **PEG** – On a PEG of 1.39, calculated on our conservative 3-year forecasts[2], Britvic is the cheapest name in our European staples coverage universe, along with Carlsberg (Figure 4)

[2] PE CY13 / EPS CAGR CY13-16E

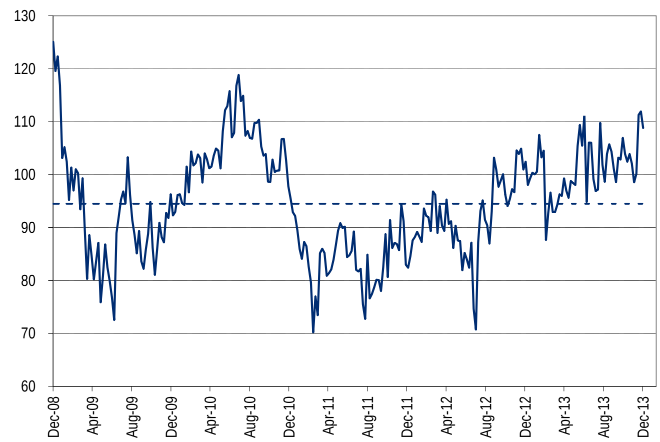
- **PEG discount to beverages** – Despite Britvic's PE re-rating, its PEG discount to the beverages sector hasn't really narrowed and is still greater than the 5 year average (Figure 5)

Figure 2. Britvic – 12 month forward PE



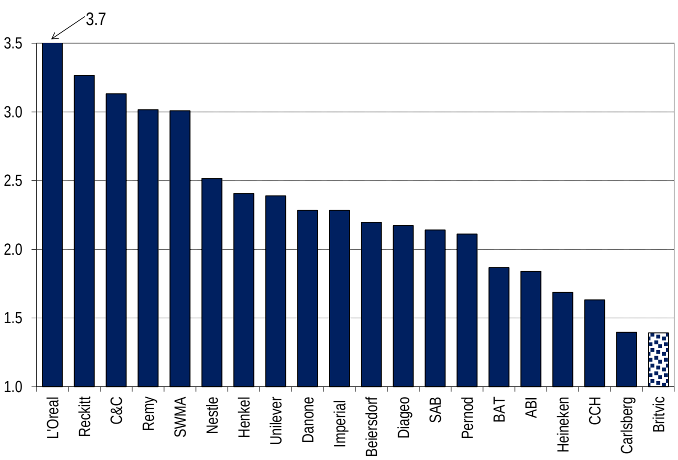
Source: DataStream, Citi Research

Figure 3. Britvic – 12 month forward PE relative to FTSE 250



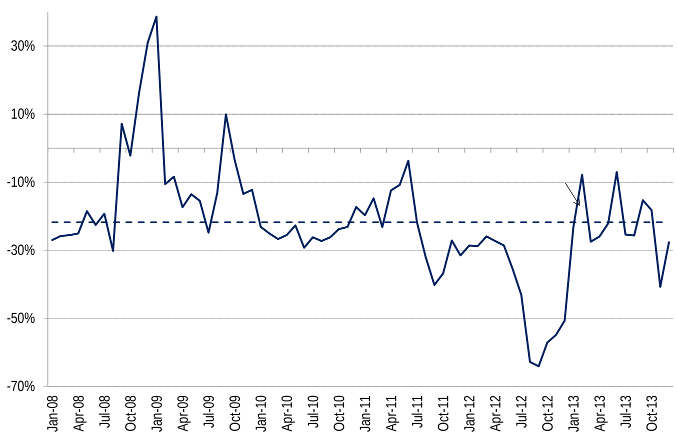
Source: DataStream, Citi Research

Figure 4. Britvic PEG vs other staples



Note: PEG = PE CY13/ EPS CAGR CY13-16E
Source: Reuters, Citi Research estimates

Figure 5. Britvic PEG discount to large cap beverages



Source: DataCentral, Citi Research estimates

- **PE CY17** – Looking out a few years and factoring in the benefit of the potential earnings upgrades, we think Britvic's valuation looks attractive. On PE CY17E, based on our conservative scenario-A, Britvic would trade on 10.8x, a 14% PE discount to the beverages sector. Under scenario B, the discount would be 26% and with scenario C it would be 32%.

Figure 6. Estimated Britvic Discount to Beverages sector on CY17 PE under our 3 earnings scenarios

	Scenario	CY17 EPS	PE CY17	discount to Beverages sector
	Existing Citi forecasts	57.2	11.7	-7%
A	Conservative	62.3	10.8	-14%
B	Medium	71.9	9.4	-26%
C	Positive	79.2	8.5	-32%

Note: CY17 EPS in this table are slightly different from the EPS in Figure 1, because those are FY EPS.
Source: Citi Research

Target price

Our 12 months target price is 850p.

We normally set our 1yr target prices based on 12-month forward multiples but, in the case of Britvic, we believe it is more appropriate to use CY17 multiples, in order to capture what we see as its good 3-year EPS growth outlook and the potential for material upgrades. Although realisation of that upside may be some years out, we think that some of the potential will be factored into the share price over the next 12 months.

We assign a 25% probability to the chance that no upside materialises and that therefore we don't end up upgrading our numbers over the next few years. And we assign 25% probability to each of the 3 scenarios we have outlined, because we believe there isn't enough visibility at this point to say whether one of them is more or less likely than the others.

- **If we end up sticking with our existing forecasts**, we believe the shares are worth 613p, because if this is the right scenario, we think the shares should be valued on a 15% PE CY17 discount to the beverages sector, slightly less than the average discount of the past few years. We believe this is justified by the fact that, even with no material upside from international, Britvic's long term growth outlook has improved whereas the outlook for the beverages sector has weakened slightly, due to the less optimistic assumptions for EMs.
- **Under scenario A**, which represents **our conservative upside forecasts,** we believe the shares are worth 746p. If this is the right scenario, we think the shares should be valued on a 5% PE CY17 discount to the beverages sector, again justified by Britvic's improved growth profile.
- **Under scenario B**, which represents our **medium upside forecasts,** we believe Britvic would be worth 951p. If this is the right scenario, we think the shares should be valued at a small premium to the beverages average CY17 PE, as Britvic's international expansion should underpin better earnings growth than that of the beverage sector in the long term.
- **Under scenario C**, which is our **positive** scenario, we believe Britvic would be worth 1,097p. If this is the right scenario, we believe Britvic should deserve an ever greater premium (10%) to the beverages sector.

Figure 7. Calculation of fair value, based on probability weighted scenarios

	Scenario	CY17 EPS	Premium to Bevs sector	CY17 PE	Value (p)	probability
	Base case (existing forecasts)	57.2	-15%	10.7	613	25%
A	Conservative	62.3	-5%	12.0	746	25%
B	Medium	71.9	5%	13.2	951	25%
C	Positive	79.2	10%	13.9	1,097	25%
	Probability weighted FV				852	100%

Source: Citi Research estimates

On this basis we get to a fair value of 852p, which we round to 850p to derive our 12 month share price target. The material difference with our previous target (640p) is explained by the fact that we now factor into our fair value the potential upside to earnings from international, further cost savings and improving UK macro.

13% EPS CAGR for the next 3 years

On our estimates, Britvic is set to deliver 13% EPS CAGR CY13-14[3]. This is:

- **Visible** – Because it is underpinned by cost savings announced last May (£30m over F14-16, of which £10m will be reinvested) and recovery from the Fruit Shoot recall in F14[4].

- **Conservative, in our view** – Stripping out cost savings, the Fruit Shoot recovery benefit and other one-offs (like the weather impact), we assume 4% (or £6m) underlying EBIT growth in FY14 and 5% thereafter, which we believe is conservative because (1) it assumes almost no volume growth and about 3.5% underlying fixed cost inflation each year and (2) it is considerably below the level of FY13, when on an underlying basis, EBIT increased 16%, or £18m (Figure 8). In FY13 however, there was a benefit from increased focus on revenue management, which is likely to be less material going forward.

Figure 8. Britvic EBIT growth drivers (£m)

	FY11	FY12	FY13	FY14E	FY15E	FY16E	FY17E
EBIT	135	113	135	156	171	184	193
Total EBIT growth		(22)	22	21	15	13	9
o/w FX		(5)	3	0	0	0	0
o/w Fruit Shoot recall Impact		(17)	7	10	0	0	0
o/w net cost savings*		8	(2)	10	7	5	0
o/w weather**		0	4.5	(4.5)	0	0	0
o/w change in mgt variable comp***		N.A	(8)	0	0	0	0
o/w underlying EBIT growth		(8)	18	6	8	8	9
underlying EBIT growth (%)		-6%	16%	4%	5%	5%	5%

Notes: *Net cost savings: in FY12 £8m exceptional PVO savings; in FY13 -£2m reinvestment in international; in FY14 £10m is the result of £13m gross savings less £3m incremental reinvestment. **Weather: the good summer boosted FY13 EBIT £4-5m, which we assume will unwind in FY14. *** Mgt variable compensation was zero in FY12 due to the Fruit Shoot recall one off. Compensation was normalized again in FY13, effectively knocking £8m off EBIT growth. Source: Company reports, Citi Research estimates

- (**Almost) best in class in European staples coverage** – We expect only CCH and Beiersdorf to do slightly better than Britvic's 13.1% EPS CAGR. The median for the European staples we cover is 8% (Figure 9). After FY16e, when we expect the benefit of Britvic's cost savings falls out, our forecasts assume high single digit EPS growth, which is as good as the large cap food names. However, there is a significant chance that growth will be faster, as the international business should start to contribute by then, but we don't really model this in our forecasts.

[3] 14% EPS CAGR FY13-16, with +19% in FY14, +13% FY15 and +11% FY16.

[4] In F14, the P&L will benefit from about £10m Fruit Shoot hit falling out (£8m quantified by management in fixed costs, but also about £2m, we believe, in brand contribution due to lost sales in FY13, non-recurring in FY14).

Figure 9. EPS CAGR (CY13-16) for European staples

	CY13-16E EPS CAGR
Coco-Cola Hellenic	14.6%
Beiersdorf	13.7%
Britvic	13.1%
Carlsberg	11.0%
AB-Inbev	10.8%
AB Foods *	10.5%
Heineken	10.1%
SABMiller	9.2%
Diageo	8.3%
Henkel	8.1%
Pernod Ricard	8.0%
Danone	7.9%
Remy Cointreau	7.9%
BAT	7.7%
Unilever	7.6%
Nestle	7.4%
L'Oreal	6.8%
Tate & Lyle	5.5%
Reckitt Benckiser	5.3%
Swedish Match	5.2%
C&C	5.0%
Imperial Tobacco	4.6%

Source: Citi Research estimates

International expansion

The greatest potential upside comes from the international expansion.

Our scenario analysis suggests the profit **from Fruit Shoot international on a multi-year view could be very material, £24-46m, on assumptions that seem reasonable, from zero today**. It could turn out to be even more than that, but equally it could be less. The reality is we don't know and the company doesn't know either.

We go through the calculations and assumptions immediately below and on page 12 we provide the background information that we believe is necessary to understand the progress Britvic has made in rolling out Fruit Shoot internationally.

Quantifying the upside for international expansion

Our existing forecasts assume that international profit will increase only by £9m between FY13 and FY17, so most of the £24-46m from Fruit shoot would be incremental.

Given the uncertainty on quantifying the upside, we outline 3 scenarios, where we make different assumptions on market shares and size/growth of the kids' juice markets. In all 3 scenarios, we assume that Britvic's EBIT margin on concentrate sales is 44% (consistent with Figure 16).

<u>Conservative scenario</u>: £24m EBIT from Fruit Shoot international

In this scenario, we assume:

- **10% share in the US market** – We assume that Fruit Shoot achieves 10% share of the $2bn kids' juice market (grocery and convenience). This seems conservative, considering that:

  1. Fruit Shoot has already achieved 20-25% share in the convenience channel in a number of the markets where it has been launched, including the Great Lakes region, Mid-Atlantic and Alabama. In France, Fruit Shoot's market share is 12% and in the UK it is 20% in the grocery channel (although it is higher in the leisure and on-premise channels).

  2. Fruit Shoot in the US is supported by Pepsi's distribution machine,

  3. We are receiving positive feedback on the brand from distributors

- **15% share in France and 10% in Spain** – In France the brand has already achieved 12% share nationally. It has just been launched in Spain through Pepsi and has been listed by most of the large retail chains. Therefore the assumption seems reasonable.

- **No growth in the size of the markets** – This is very conservative, in our view, because per cap consumption of kids' juice in the US is about 1/3 of the UK level and in France it is less than 1/4 of the UK level. It is likely that Britvic's innovation and, potentially, some form of competitive response and/or development of me-too products will help grow the market, recruiting kids from less healthy carbs drinks.

- **No new market entries** – In our conservative scenario we don't assume Britvic will enter any new market and we assume zero profit for India.

Figure 10. Kids' Juice markets and per capita consumption

	UK	US	France
Size of the market (retail prices, USD mln)	1,143	2,000	274
Population (mln)	64	317	66
Per cap consumption (USD)	18	6	4

Source: Company Reports, Citi Research estimates

Figure 11. Potential upside from Fruit Shoot international: CONSERVATIVE scenario - £24m EBIT (FY17)

	US	France	Spain*	Other
Size of market (retail prices, USD)	2,000	280	199	
Size of market (bottler selling prices, USD)	1,399	196	139	
Size of market (bottler selling prices, GBP)	858	120	86	
Fruit Shoot market share	10%	15%	10%	
Fruit Shoot sales	86	18	9	
Britvic concentrate sales (est 50% of bottler sales)	43			
Britvic EBIT margin	*44%*	*20%*	*15%*	
Britvic EBIT	19	4	1	0

Note: We don't know the size of the market for Spain, so we have assumed similar per cap consumption to France.
Source: Citi Research estimates

<u>Positive scenario</u>: £46m EBIT from Fruit Shoot international

Our assumptions here are more optimistic, but nevertheless realistic, we believe.

- **15% market share in the US –** This is still below the level achieved so far in a number of regions where Fruit Shoot has launched.
- **20% share in France and Spain**
- **5-6% growth per annum in the markets** – As we said above, kids' juice per cap in the US and France is much lower than in the UK, so we would expect Fruit Shoot's entry to help grow the market. Therefore we assume 5% growth in per cap consumption every year + 0.7% population growth in the US (0.5% in France and 0% in Spain). Over 4 years, this means the market would grow about 30%.
- **£2m profit from new market entries** – This could be India, further growth in the Netherlands, or any new market entry. Therefore, if anything, £2m seems conservative.

Figure 12. Upside from Fruit Shoot international: MORE POSITIVE scenario – £46m EBIT (FY17)

	US	France	Spain*	Other
Size of market (retail prices, USD)	2,496	347	242	
Size of market (bottler selling prices, USD)	1,746	243	169	
Size of market (bottler selling prices, GBP)	1,071	149	104	
Fruit Shoot market share	15%	20%	20%	
Fruit Shoot sales	161	30	21	
Britvic concentrate sales (est 50% of bottler sales)	80			
Britvic EBIT margin	44%	20%	15%	
Britvic EBIT	35	6	3	2

Note: We don't know the size of the market for Spain, so we have assumed similar per cap consumption to France.
Source: Citi Research estimates

<u>Medium scenario</u>: £39m EBIT from Fruit Shoot international

The assumptions we make here are in between the conservative and positive scenarios.

We assume: (1) 12.5% US share, (2) 20% share in France and Spain, (3) 3% growth in kids juice markets (vs 5-6% in the positive scenario) and (4) no profit from other markets.

Other scenarios

As we said, the assumptions we have made are arbitrary, although we believe they are reasonable. We could construct an "even more positive scenario", assuming for instance (1) 20% share in the US, (2) 5-6% growth in the markets and say (4) £5m profit from new market entries. In this case the total EBIT from international would be **£61m**.

Impact on EPS boosted by low tax rate in Ireland

The EBIT upside estimated in all the scenarios is largely incremental to our forecasts (and to consensus), as we have international profits increasing by £9m over the next 4 years and we don't assume anything in our model specifically for Fruit Shoot in France.

12.5% tax rate on international profit

Moreover, because Fruit Shoot concentrate manufacturing is based in Ireland, most of Britvic's international profits are likely to be subject to the low Irish corporation tax rate (12.5%).

International expansion so far

We estimate that total Fruit Shoot retail sales are about £260m, of which around 1/3 are outside the UK. The main markets are France (about £20m estimated retail sales), the US (£10-20m) and the Netherlands (around £10m). The brand has recently been launched in Belgium (2011), Spain (2013) and will be launched in India in summer 2014.

The US

Fruit Shoot was first launched in the US in 2008 in Alabama, through Buffalo Rock, Pepsi's fourth largest independent bottler. Since then it has made huge progress.

- **41 states** – Fruit Shoot is now in 32 states, with distribution in 9 more commencing in 2014, which will take the total to 41, representing nearly 80% of the US population. The large states that are still missing are California, Illinois and Michigan. <u>It is just a question of time, we believe, before Fruit Shoot goes national</u>.
- **Agreements with all major Pepsi bottlers** – After Buffalo Rock, the brand has been taken on by: Gross & Jarson (the 3rd largest Pepsi bottler), Pepsi Bottling Ventures (the 2nd largest), Pepsi Bottling Company and, most importantly, Pepsi Americas Beverages (PAB), Pepsi's fully owned bottling subsidiary, which distributes 75% of Pepsi's US volume.
- **15 year agreement** – In November 2013, PAB committed to a 15 year agreement with Britvic, which is unusual for Pepsi, implying it has high expectations for Fruit Shoot. We have had very positive feedback from distributors too.

- **Franchise model** – Since 2012 the model has shifted from a finished goods to a franchise model. Britvic supplies the concentrate from Ireland and the bottlers manufacture and distribute the finished product. Unlike Britvic's UK and Ireland EBAs with Pepsi, in the US Britvic takes care of the marketing costs.
- **2 manufacturing sites** – Fruit Shoot is currently manufactured in one plant (owned by PBV) in North Carolina, and a second facility (owned by PAB) in St Louis will start production in 2014.
- **Entirely single serve, for now** – Fruit Shoot is exclusively sold in single-serve format, mostly in gas stations and convenience stores. Fruit Shoot is now in 60,000 points of sale. Management has quantified the **convenience channel for the kids' juice market (nationally) at $200m retail sales.**
- **Listings with key customers** – Fruit Shoot has achieved listings with a number of major grocers, including, WalMart, Kroger, Dollar General, Hess, where for now it only sells in single-serve format, as we said. It recently announced a contract with Legoland in Florida, which will provide a good visibility platform for the brand.
- **Testing multi-pack – The grocery/multi-pack channel portion of the kids' juice market is worth $2bn**. It is just a question of time, we believe, before Fruit Shoot moves to multi-pack. To ensure a successful roll-out, Britvic needs to (1) achieve national distribution, as this is what the retailers want, (2) ensure the supply chain works flawlessly and at some point add further capacity, we believe, (3) make sure it gets the price/pack architecture right and, for this, it is currently testing multi-packs with Buffalo Rock in Alabama.
- **20-25% share in some of its markets –** Fruit Shoot has achieved 20%+ market share in its established US states and a similar level in some of the more recent areas.

Figure 13. Fruit Shoot in France

	GBP mln
Kids' Juice drinks market	158
Fruit Shoot retail sales	19
market share	12%

Source: Britvic, Citi Research

France

Fruit Shoot was launched in France in 2011 and has achieved 12% share in a kids' juice market worth around €200m. Britvic markets the finished product in France directly through the Fruité network and, differently from the US, Fruit Shoot is sold primarily in the grocery channel, leveraging Fruité's relationships with the retailers. Up until now, Fruit Shoot has been supplied from the Norwich plant, but as from 2014 it will be manufactured in the South of France.

Benelux

Retail sales in the Netherlands are above €10m. More recently the brand was launched in Belgium too. The finished product is supplied from the UK.

Spain

Fruit Shoot was launched in Spain earlier this year through Pepsi Spain, with a finished product model. It has secured listings in 4 of the 6 major national grocery chains plus a number of regional chains. We believe retail sales in Spain amount to a few million Euros for now.

India

A few months ago Britvic announced a distribution agreement with Narang for a mid-2014 Fruit Shoot launch. The product will be manufactured locally by a 3rd party supplier to whom Britvic will supply the concentrate. Fruit Shoot in India will target the middle class, therefore a potential of 60-100 million consumers. From a distribution point of view, the launch will focus on the large cities with about 100k target points of sales. Once manufacturing is up and running, India could potentially supply other markets in the region, should Britvic decide to enter them.

Australia

Britvic launched Fruit Shoot in Australia in November 2010 through a franchise agreement with Bickford's, a local soft drinks player. To date Australia hasn't quite lived up to expectations, which could be due to a number of factors: (1) the deal seemed to be done rather opportunistically, with Bickford's approaching Britvic, we understand. Bickford's is a relatively small player, therefore possibly not the right partner for Fruit Shoot, particularly given the difficult retail environment; (2) the launch hasn't been staffed as well as other international launches. Britvic doesn't have any of its people on the ground in Australia, unlike in the US, where it has 24 staff.

Future market entries

Over time, the plan is to enter new markets, clearly not all at once, given (1) the importance of choosing the right partner and (2) the launch costs (it takes about 3 years for an international launch to break-even, according to management).

Britvic sees its addressable kids, family and adults market being worth over $30bn globally.

- **Which markets?** In our opinion, the markets Britvic may decide to enter are more likely to be ones where there is an existing kids' juice market or a developed dilutables market, where in the long term Britvic should be able to leverage its other brands, Robinsons and Teissere. Besides a number of Western European markets, the largest dilutables markets where Britvic is not already present are: South Africa, Mexico, Argentina, Brazil and Indonesia (Figure 14).

- **With what partners?** Britvic's international expansion is mostly going to be "asset light", ie with local partnerships (similar to the US, Spanish and Indian models). We expect the preferred partner would be Pepsi, unless they are not present in a given market, not strong enough or not interested. Management, however, doesn't rule out acquiring businesses (or taking a stake in a business) that could provide strong brands and/or route-to-market in new countries. These would have to be in Britvic's core categories: family, kids and adults.

Figure 14. Top-15 concentrates markets – 2012

	Volume Mn Litres	Value $ bn
United Kingdom	432	1.1
South Africa	262	0.4
France	225	1.2
Mexico	209	2.0
Argentina	206	0.8
Brazil	161	2.7
Australia	128	0.3
Indonesia	95	0.8
Netherlands	57	0.2
Japan	46	0.6
Ireland	44	0.1
Sweden	41	0.2
Poland	40	0.2
Czech Republic	38	0.1
India	37	0.1

Source: Euromonitor, Citi Research

The economics of the concentrate model

Before we attempt to assess the international potential for Fruit Shoot, we illustrate the assumptions we make on the franchise relationship with Pepsi bottlers.

- **The bottler's P&L** – Britvic knows the cost structure of Fruit Shoot, so it can price the concentrate in order to leave the bottler earning an attractive EBIT margin, we believe, of about 15%. Besides the concentrate cost, the bottler has to incur other raw material and packaging costs, production bottling costs, no marketing (as this is covered by Britvic) and very limited incremental G&A and distribution costs, as it distributes Fruit Shoot to its existing customers, with its existing trucks.

Figure 15. Bottler's P&L for Fruit Shoot

	USD	%
Retail price	1.00	
Bottler Net sales (net of sales tax and retail mark-up)	0.70	100%
Concentrate Cost	-0.35	-50%
Other Cost of Goods	-0.23	-33%
Gross Profit	0.12	17%
Marketing	0.00	0%
Brand Contribution	0.12	17%
Incremental G&A and distribution	-0.02	-3%
Bottler EBIT margin (10-15%)	0.10	14%

Source: Citi Research estimates

- **Britvic's P&L** – Britvic's revenue is the concentrate sales (the main cost for the bottler). Concentrate gross margins are normally very high, depending on the price at which concentrate is charged to the bottler. For Fruit Shoot, we believe the price will be quite high (around 50% of the end value of the product), reflecting the fact that Britvic incurs the marketing costs. Therefore we calculate a gross margin of about 70%. Incremental G&A and distribution cost for Britvic are not material, given the asset light franchise model.

- **22% EBIT margin on the end product** – Based on our assumptions, we estimate that Britvic will probably earn a margin of 20-25% on the value of the final product (bottler prices). Calculated on concentrate sales, Fruit Shoot's EBIT margin is close to 45%, we believe. The margin isn't at this level yet, however, given the higher A&P costs (as a pct of sales) in the early phases of the launch.

Figure 16. Britvic P&L on Fruit Shoot concentrate sales

	USD	cost structure on concentrate sale	% (on finished good sales price of $0.70)
Net sales (concentrate sales)	0.35	100%	50%
Cost of Goods	-0.10	-30%	-15%
Gross Profit	0.24	70%	35%
Marketing	-0.06	-16%	-8%
Brand Contribution	0.19	54%	27%
Incremental G&A and distribution	-0.03	-10%	-5%
Britvic EBIT margin	0.15	44%	22%

Source: Citi Research estimates

There is scope for more cost savings

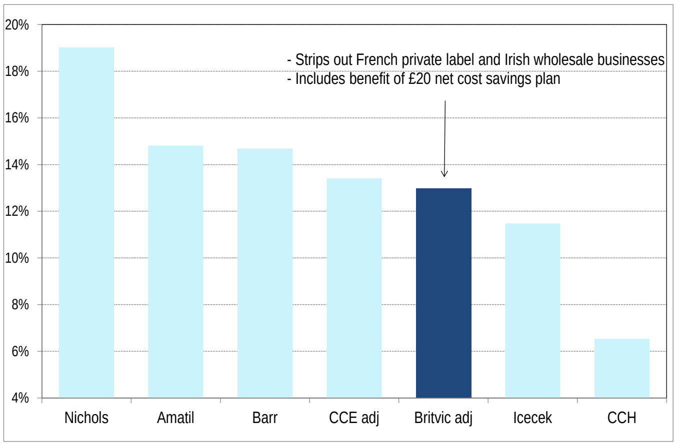
We believe there is scope for further cost savings in the medium term.

The current £30m cost savings plan should lift Britvic's EBIT margin to about 12%, or close to 13% if we adjust to strip out the low margin French private label and Irish wholesale operations.

While, at 13%, Britvic's EBIT margin is close to the level of CCE and above other European bottlers' (Figure 17), we believe it should be higher:

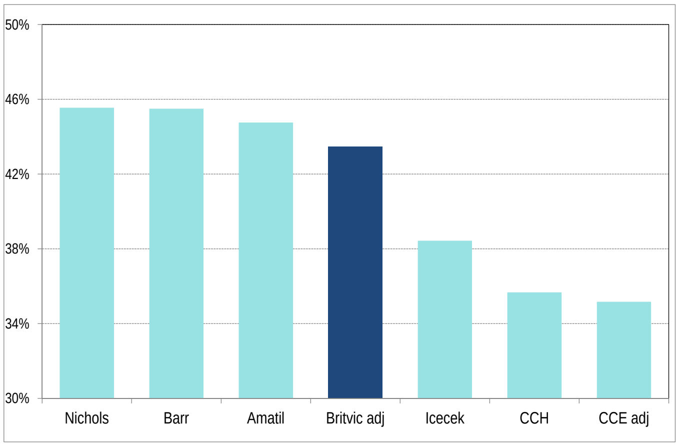
- **Britvic's gross margin is and should be above the level of European bottlers**[5], as we show in Figure 18, reflecting the fact that a higher portion of Britvic's sales comes from (1) owned brands and (2) stills.
- **However, Britvic's SG&A costs seem too high relative to peers.** Figure 19 shows that with the exception of AG Barr (which is 1/5 of the size of Britvic), Britvic's SG&A as a percentage of sales are the highest among the peer group.
  - CCE's lower SG&A/sales ratio is partly justified by its size, which should drive greater economies of scale, although we note that its business is spread over 6 countries, which mitigates the scale advantage
  - On this basis, however, Britvic's SG&A should be more materially lower than AG Barr's
  - Comparing admin costs for the companies we have data for (including a few UK-centric food companies), Britvic ranks poorly (Figure 20).

Figure 17. EBIT margins – peer comparison



Note: For Britvic, CCH, CCE we use FY13e (Citi estimates), for the other companies we use the latest reported FY. Britvic is adjusted to (1) strip out Irish wholesale and French private label and (2) include the benefit of current cost savings plan. CCE's margin is also adjusted to include the benefit of its current cost savings plan.
Source: Company reports, Citi Research estimates

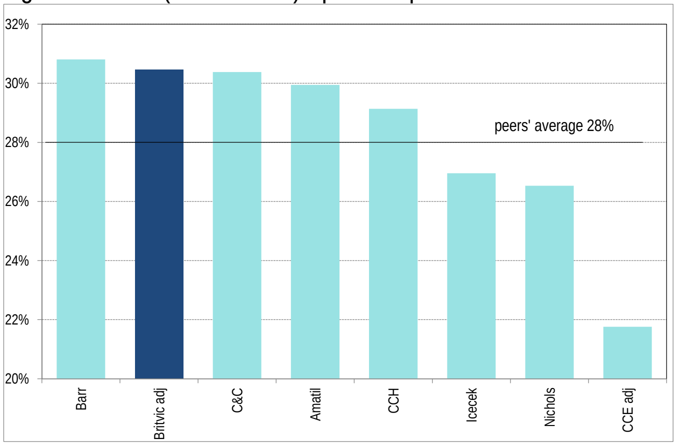
Figure 18. Gross margins – peer comparison



Note: refer to Figure 17. Source: Company reports, Citi Research estimates

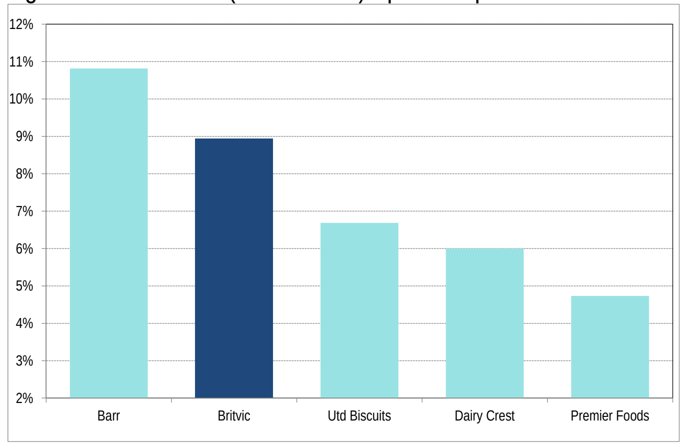
[5] We note that there could be some differences in the ways companies report COGS and gross profit. For Britvic, we have calculating gross profit/margin by adding back A&P to brand contribution.

Figure 19. SG&A (as % of sales) – peer comparison



Note: refer to Figure 17. Source: Company reports, Citi Research estimates

Figure 20. Admin costs (as % of sales) – peer comparison



Note: For Britvic, CCH, CCE (CCE.N; US$41.11; 2) and Premier Foods (PFD.L; £1.26; 2H) we use FY13e (Citi estimates), for the other companies we use the latest reported FY. In this chart Britvic is not adjusted to strip out private label and wholesale. And we haven't included the benefit of current cost savings, because we don't know the slit within fixed costs. Source: Company reports, Citi Research estimates

We don't have enough data to be more specific, but based on the above we think it is reasonable to assume that Britvic could reduce its SG&A/sales ratio further.

The average ratio for Britvic's peer group is 28%, so it doesn't seem unreasonable to assume that over time Britvic could move towards this level, from 30.5%, which is where we estimate its ratio will be once the current cost savings have been delivered and adjusting to strip out the low margin French private label and Irish wholesale businesses.

This would mean up to £33m of potential gross cost savings beyond the current plan. Assuming 2/3 retention rate (in line with the existing cost savings plan), this would lift Britvic's EBIT margin to about 14% (or 15% excluding French private label and Irish wholesale, which hold back group margin by about 80bps, we calculate) and it would drive up to £20m benefit to EBIT.

Supporting our view that there is scope for further cost savings:

- Management has hinted at the fact that the current cost savings plan is conservative, making it clear that £30m is a very "secure" number.
- We believe the plan was put together in a fairly short period of time and designed in a top-down way, as Britvic needed to come up with an alternative to the proposed Barr merger. The plan announced in May didn't in fact contain much detail in terms of procurement and route-to-market savings.
- £30m savings feels a low number, given the significance of the projects that underpin it.
  - 10-15% staff reduction (330-490 employees): this alone should save £14-21m
  - Closing-down two UK facilities (with 7% reduction in number of production lines) and one distribution depot. Most of these savings should be captured in the staff reduction figure, but not all.
  - Efficiencies in procurement, through implementation of strategic sourcing programs and consolidation of indirect supplier base. A mere 2% benefit on raw material and packing costs would be worth £12m.
  - Elimination of complexity by combining GB and Ireland support functions. We believe the savings here go well beyond staff reduction
  - "Fundamentally changing the Irish business model"

  Improved efficiency of UK route-to-market, with fewer resources servicing small accounts

Improving UK macro

Management has said that the improving macro has not had any impact on the business so far. Indeed, in September the soft drinks industry was down.

Britvic's FY14 guidance does not assume a macro benefit and we don't really factor it into our forecasts either. However, we believe the risk is on the upside.

- Our Citi Economists expect the UK to have materially better GDP in 2014 and 2015. Interestingly, the UK is expected to have the highest GDP growth among G7 countries in 2014 and 2015 (Figure 21).

- Our retail colleagues expect UK household available cash[6] to increase by 3.6% in 2014 and by 3.9% in 2015, the highest YoY growth levels in 10 years bar 2010[7] (Figure 22).

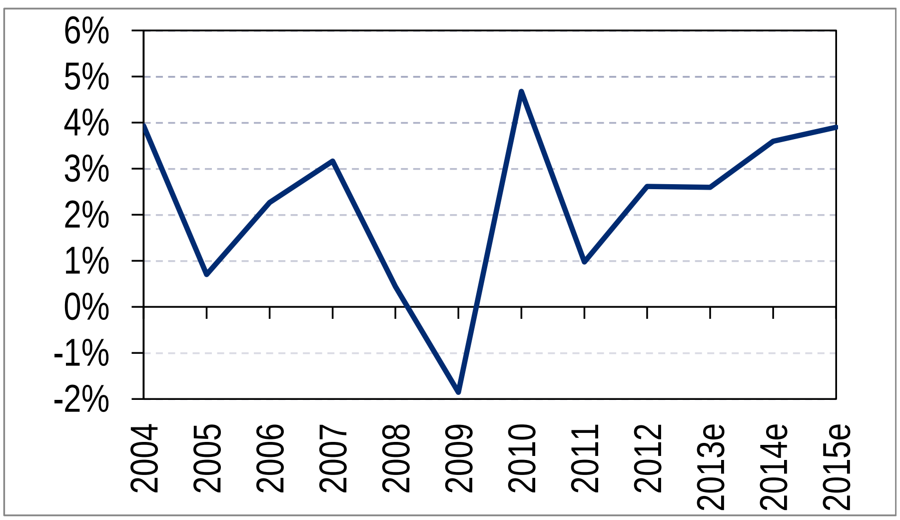
Moreover, a benign input cost outlook should help too. Management has guided to low-single-digit inflation, but if anything we think this could be a bit conservative.

Figure 21. GDP growth in G7 countries

	2012	2013E	2014E	2015E
UK	0.1%	1.5%	3.2%	3.2%
France	0.0%	0.2%	0.8%	0.9%
Germany	0.9%	0.5%	1.9%	1.7%
Italy	(2.4%)	(1.8%)	0.2%	0.3%
US	2.8%	1.7%	2.7%	3.1%
Japan	2.0%	1.8%	1.6%	0.9%
Canada	1.6%	1.7%	2.4%	2.7%

Source: Citi Economics Research

Figure 22. UK Household available cash (YoY % change)



Source: ONS, Bank of England, Citi Research

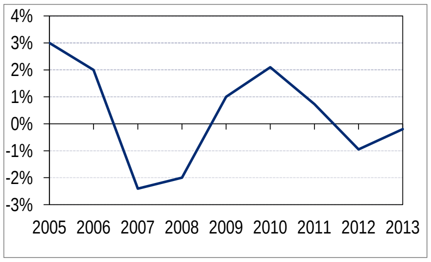
[6] Our retail colleagues' proprietary " household available cash" (HAC) is calculated as the discretionary cash flow available to consumers after fixed costs, such as rent/mortgage payments, food, energy bills, etc. For more detail please refer to their recent report "Santa Claus Is Coming To Town".

In 2010, the last time the UK macro environment was reasonably benign and input cost inflation was very moderate too, Britvic's GB brand contribution increased £45m in absolute terms, or +15%, and the margin was up 230bps, as we show in Figure 28.

The impact of the better macro environment could be slightly better volume growth and more favourable channel mix.

Better UK macro could drive volume improvement…

Figure 23. UK Soft Drinks volume growth



Source: Britvic, Citi Research. Note: for 2013 we have stripped out an estimated 1.5% weather benefit

In the past 3 years volume growth for the soft drinks industry has ranged between -1% and +1%, as shown in Figure 23.

However in 2010, the last year HAC was strong, industry volumes grew 2% and prior to the recession the UK soft drinks industry had tended to grow at 2-3% per annum, with variations depending on the weather. Indeed, Britvic's medium term guidance, provided in 2009 (and reiterated in March-12), was based on this too.

Therefore, it is conceivable that 2014-15 soft drinks volumes could improve over the recent trend, with the caveat that there will be a difficult weather comp next summer.

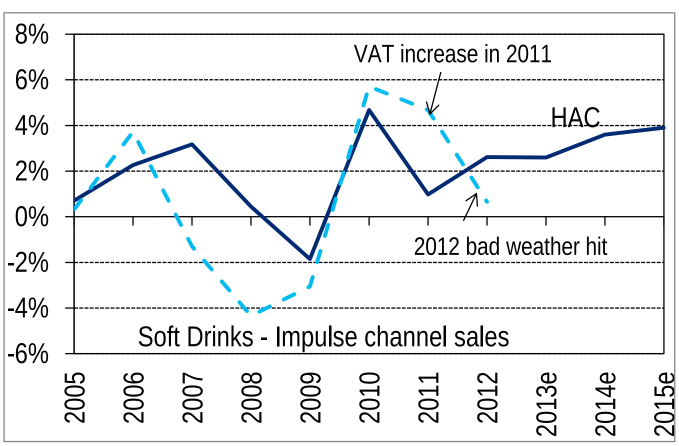
… and favourable channel mix

A stronger macro environment should drive an improvement in on-premise and impulse channel sales, which represent about 15% and 20% respectively of Britvic GB sales. This can be seen in Figure 26, where we estimate Britvic's GB sales split by brand and by channel.

Historically, there has been a reasonably good correlation between household available cash and sales in the impulse and in the pubs & clubs channels, where consumer spend is more discretionary than in grocery (Figure 24 and Figure 25).

Indeed, going back 10 years, the impulse channel had its best year in 2010, when household available cash grew 4.7%. The on-premise channel also materially recovered in 2010.

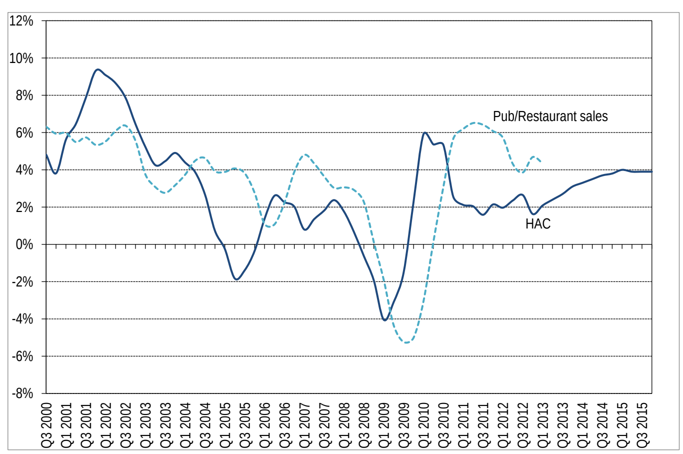
Figure 24. UK Soft Drinks Impulse channel sales vs household available cash (YoY % change)



Note: Soft Drinks impulse channel sales adjusted to include only subcategories where Britvic is present. The category is weighted according to Britvic's sub-category exposure.

Source: Citi Research, Britvic Soft Drinks Review

Figure 25. Pubs and Restaurant sales vs household available cash (YoY % change, 3 quarters smoothed average)



Source: Citi Research, ONS

A channel shift towards on-premise and impulse is positive for Britvic's ARP (price/mix) and margins, because:

- **Positive pack mix**: on premise and impulse channel sales skew to single-serve, which has a much higher average price per unit compared to multi-pack.
- **Positive brand mix**: Britvic sells relatively more J2O in the pubs and more Mountain Dew in the impulse channel. Both products are relatively highly priced.
- We believe Britvic's pricing terms are overall more favourable in the impulse and on-premise channels than with the supermarkets.
- In the on-trade, in particular, we estimate that over 50% of Britvic's sales are own brands, which carry higher margins than the Pepsi franchise brands.

Figure 26. Britvic GB – Estimated sales split by brand and channel (2013)

	Pubs & Clubs	Grocery	Impulse	Food Service	Total
Pepsi	58	170	88	82	398
Robinsons	0	113	5	0	118
Fruit Shoot	9	70	9	25	113
J20	35	35	2	3	75
Tango	5	13	10	6	34
Mountain Dew	2	5	20	3	30
R Whites	18	4	2	4	28
7 UP	5	10	5	3	23
Drench	2	1	10	6	19
Britvic Mixers and Juices	10	4	1	0	15
Lipton	0	5	3	0	8
SoBe	0	3	4	0	7
Gatorade	0	3	1	0	4
other	1	1	2	0	4
Total	144	438	162	131	876
Channel split	16%	50%	19%	15%	100%

Source: Citi Research, company reports

FY14 input cost outlook is favourable too

Management has guided to low single digit input cost inflation, with flattish underlying costs and some negative FX impact, as certain commodities are sourced in Euro, which has strengthened over the pound.

We believe this guidance could, if anything, be slightly conservative. We don't have a clear insight into the prices that management has negotiated for each commodity and indeed juice price negotiations are still ongoing, but our analysis suggests that, on an underlying basis, input costs should be down slightly, not flat. And this wouldn't surprise us, as companies tend to keep a low profile when input costs are going down, given their pricing negotiations with the retailers.

Figure 27. Britvic – GB input cost breakdown and FY14 estimate

Raw Material	% of GB prime costs	Comment	Currency	FY14 est inflation
Concentrate	28%	Purchased from Pepsi on an annual basis at a price linked to RPI	GBP	up ~2%
Juice	15%	Negotiations ongoing. Mgt expects juice costs to be flat	USD	flat
Glass	6%	Linked to energy prices, therefore up more than inflation	GBP	up MSD
PET	10%	Half hedged	EUR	down MSD
Steel	10%	Mgt hasn't commented on steel	GBP	DD decline
Sugar	15%	Mangement has said that sugar prices are well down	EUR	MSD decline
Other	16%	Includes emulsifiers, citric acid, plastic caps and closures		
Total underlying inflation (Citi estimates)				down about 1%
FX impact				1.5%
Total input cost inflation				flat to +0.5%

Source: Company data and Citi Research estimates

Macro and input cost tailwinds could drive up to £9m profit uplift

We think our current GB forecasts are reasonably conservative. In fact we assume:

- Broadly flat underlying volume growth (ex Fruit Shoot and weather distortions) in FY14 and +1% in FY15
- 2% price/mix (ARP) in FY14 and +2.5% in FY15, underpinned by management's focus on improving promotion effectiveness. To put this into context, in FY13 stills ARP increased 7% and carbs ARP was up 3.5%.
- £14m underlying brand contribution increase in FY14 and £16m in FY15, which is +4% (vs +5% in FY13).

As we said, our economists expect UK households to have more cash for discretionary spend in 2014 (+3.6%) and in 2015 (+3.9%), therefore we believe it is reasonable to assume that soft drinks sales could benefit too.

In 2010, when HAC increased 4.7% and the input cost environment was favourable too, Britvic's GB brand contribution increased £45m (+15%), but it is fair to note that in 2010 Britvic also enjoyed particularly good growth in the impulse channel, as it rolled out the 600ml bottle and Mountain Dew.

Figure 28. Britvic GB operational metrics (sales and brand contribution) vs input cost inflation and UK household available cash

	FY08	FY09	FY10	FY11	FY12 adj	FY13 adj	FY14e adj	FY15e	FY16e
GB Carbs sales growth (%)	4%	11%	12%	7%	3%	3.6%	3.0%	3.5%	3.2%
GB Stills sales growth (%)	5%	6%	4%	-3%	-3%	2.1%	-0.1%	3.5%	3.1%
Tot GB sales growth (%)	4%	8%	8%	3%	1%	2.4%	2.3%	3.5%	3.2%
Tot GB sales growth (£ mln)	30	60	64	23	5	20	20	32	30
GB Brand contribution growth (£ mln)	(1)	17	45	(13)	(1)	15	14	16	15
GB Brand contribution growth (%)	0%	6%	15%	-4%	0%	4.6%	3.9%	4.3%	3.9%
Margin change (bps)	(194) bps	(94) bps	229 bps	(269) bps	(40) bps	84 bps	65 bps	29 bps	31 bps
Input cost inflation	4.0%	4.0%	0-1%	10.0%	MSD	LSD	0-1%		
Household Available Cash	0.4%	-1.9%	4.7%	1.0%	2.6%	2.8%	3.6%	3.9%	

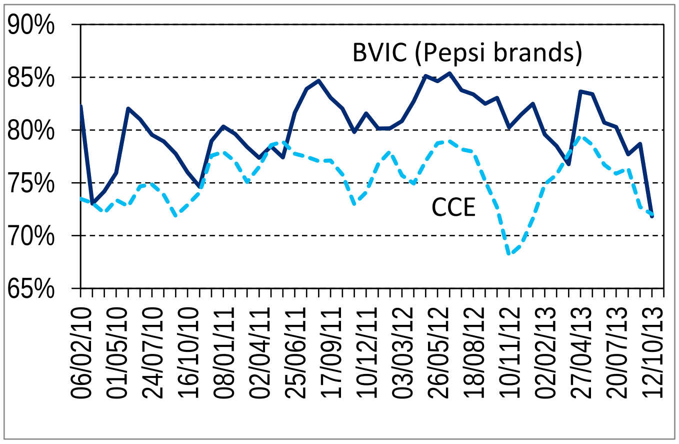
Note: FY12, FY13 and FY14 sales and brand contribution have been adjusted to strip out (1) Fruit Shoot recall distortions, (2) The 2013 summer weather impact and (3) our estimate of cost savings benefit to Fy14 brand contribution. Source: Company Reports, Citi Research estimates

If we assume 1pp better sales growth (0.5% volume and 0.5% mix) in FY14 and in FY15 (both in stills and carb), which means Britvic GB sales growth would be 3.5% in FY14 and 4.5% in FY15 4-5% (vs a long term 4-6% target), **the cumulated impact on FY15 brand contribution and EBIT would be about £9m** positive (and the impact on EPS +6%). In a less optimistic scenario, we suggest the upside could be half of that, £4.5m.

What could go wrong, besides the better macro not driving an uplift in consumer spend?

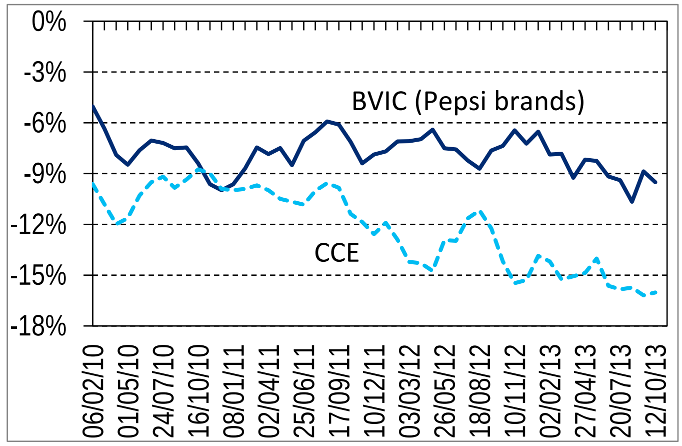
The competitive environment in carbs remains very intense and is showing no signs of improvement. However, comparing the current situation with that of 2010, there isn't a huge difference, as the following charts illustrate.

Figure 29. UK Carbs – % of volume sold on promotion (BVIC vs CCE), 3 months moving average



Source: Nielsen (grocery channel), Citi Research

Figure 30. UK Carbs – average promotional price vs full price (BVIC vs CCE), 3 months moving average



Source: Nielsen (grocery channel), Citi Research

Financial Summaries

Figure 31. Britvic -- Financial Summary, FY08-FY17E (£ in millions)

Profit and Loss / Yr. to Sep	2009	2010	2011	2012	2013	2014E	2015E	2016E	2017E	2018E	5yr CAGR
Net Sales	979	1,139	1,290	1,256	1,322	1,355	1,403	1,450	1,500	1,555	3.3%
EBITDA	148	179	184	157	179	201	218	233	245	258	7.6%
Margin	*15.2%*	*15.7%*	*14.2%*	*12.5%*	*13.5%*	*14.9%*	*15.5%*	*16.1%*	*16.4%*	*16.6%*	*3.1%*
Group EBIT	110	135	135	113	135	156	171	184	193	204	8.6%
Margin	*11.2%*	*11.8%*	*10.5%*	*9.0%*	*10.2%*	*11.5%*	*12.2%*	*12.7%*	*12.9%*	*13.1%*	*2.9%*
Net Finance	(24)	(26)	(30)	(28)	(27)	(25)	(22)	(20)	(16)	(13)	-13.3%
Pretax Profit	87	109	105	84	108	132	149	165	177	191	12.1%
Exceptionals (Pretax)	(20)	(138)	(25)	(7)	(26)	(30)	(20)	0	0	0	
Tax	(19)	(19)	(22)	(20)	(21)	(24)	(30)	(38)	(40)	(42)	
Underlying Tax Rate	29.3%	67.4%	26.9%	25.9%	25.1%	24.0%	23.5%	23.0%	22.5%	22.0%	
Minorities	0	0	0	0	0	0	0	0	0	0	
Adjusted Net Profit	66	82	81	66	86	103	117	130	140	152	12.2%

Per-Share Data / Yr. to Sep	2009	2010	2011	2012	2013	2014E	2015E	2016E	2017E	2018E	5yr CAGR
EPS (Adjusted, diluted)	29.8	35.5	32.9	26.5	35.0	41.8	47.2	52.2	56.1	60.7	11.6%
DPS	15.0	16.7	17.7	17.7	18.4	20.4	23.1	25.6	27.6	29.9	10.2%
Number of Dil. Shares Out	221	232	246	249	245	247	248	249	250	251	0.5%

Growth Rates (%) / Yr. to Sep	2009	2010	2011	2012	2013	2014E	2015E	2016E	2017E	2018E	5yr CAGR
Volume	4%	13%	7%	-2%	0%	0%	1%	1%	1%	1%	0.9%
Sales	6%	15%	15%	-3%	5%	2%	4%	3%	3%	4%	3.3%
EBIT	13.4%	22.7%	0.3%	-16.5%	19.8%	15.8%	9.3%	7.8%	4.9%	5.7%	8.6%
EBITDA	6.5%	20.6%	2.6%	-14.7%	14.1%	12.7%	8.2%	7.1%	5.1%	5.2%	7.6%
Profit before Tax	23.4%	26.1%	-3.7%	-19.7%	28.1%	21.7%	13.1%	10.7%	7.4%	8.1%	12.1%
Net Profit	20.5%	24.7%	-1.5%	-18.5%	29.8%	20.3%	13.4%	11.1%	7.9%	8.6%	12.2%
EPS	18.9%	18.9%	-7.3%	-19.3%	32.0%	19.2%	12.9%	10.7%	7.5%	8.2%	11.6%

Cash Flow / Yr. to Sep	2009	2010	2011	2012	2013	2014E	2015E	2016E	2017E	2018E	5yr CAGR
Operating Cash Flow	150	146	146	145	153	166	204	220	232	245	9.9%
Interest	(25)	(25)	(31)	(29)	(27)	(25)	(22)	(20)	(16)	(13)	
Tax	(19)	(22)	(21)	(13)	(11)	(16)	(21)	(28)	(32)	(34)	
Capex	(38)	(40)	(37)	(44)	(26)	(67)	(47)	(50)	(55)	(55)	15.9%
Free Cash Flow	67	59	57	60	89	58	114	122	129	143	10.0%
Margin	*6.9%*	*5.2%*	*4.4%*	*4.8%*	*6.7%*	*4.3%*	*8.1%*	*8.4%*	*8.6%*	*9.2%*	
M&A	10	(147)	(5)	2	0	0	0	0	0	0	
New Equity	(3)	93	(1)	(7)	7	(8)	(7)	(8)	(9)	(9)	
Change in Cash Items	34	(40)	(1)	7	45	(4)	49	50	50	59	
Non-Cash Items	(44)	(65)	(13)	12	8	0	0	0	0	0	
Change in Net Debt	(10)	(105)	(14)	19	53	(4)	49	50	50	59	
End of Year Net Cash/(Debt)	(411)	(516)	(530)	(512)	(458)	(463)	(413)	(364)	(314)	(255)	

Ratios / Yr. to Sep	2009	2010	2011	2012	2013	2014E	2015E	2016E	2017E	2018E
Interest Cover	4.6	5.3	4.5	4.0	5.0	6.3	7.7	9.4	11.8	15.5
Dividend Payout	0.50	0.47	0.54	0.67	0.53	0.49	0.49	0.49	0.49	0.49
Adj. Net Debt/EBITDA	2.8	2.5	2.5	2.9	2.3	2.0	1.6	1.3	1.0	0.8
ROIC	19.2%	20.8%	19.7%	16.9%	21.1%	23.8%	25.6%	27.7%	29.2%	0.0%

Historical Multiples / Yr. to Sep	2009	2010E	2011	2012	2013	2014E	2015E	2016E	2017E	2018E
Historical Average Share Price (p)	264	439	411	340	458	672	672	672	672	672
Historic Mkt Cap	567	987	987	823	1,115	1,647	1,654	1,661	1,667	1,674
P/E	8.8	12.4	12.5	12.8	13.1	16.1	14.2	12.9	12.0	11.1
Dividend yield	5.7%	3.8%	4.3%	5.2%	4.0%	3.0%	3.4%	3.8%	4.1%	4.5%
FCF Yield	11.9%	6.0%	5.8%	7.3%	8.0%	3.6%	6.9%	7.3%	7.7%	8.6%
Historic EV	1,028	1,552	1,592	1,368	1,612	2,127	2,111	2,068	2,025	1,978
EV/EBITDA	6.9	8.7	8.7	8.7	9.0	10.6	9.7	8.9	8.3	7.7

Source: Company Reports and Citi Research Estimates

Figure 32. Britvic -- Divisional Summary, FY08-FY17E (£ in millions)

Sales / Yr. to Sep	2009	2010	2011	2012	2013	2014E	2015E	2016E	2017E	2018E	5yr CAGR
GB Stills	350	363	351	322	340	347	359	370	382	393	2.9%
GB Carbs	417	468	503	518	536	553	572	591	610	632	3.3%
International	22	26	29	29	38	45	51	58	65	73	14.2%
Ireland	190	179	163	139	137	135	138	141	145	149	1.7%
France	-	85	245	249	271	275	283	290	299	308	2.6%
Total Sales	979	1,121	1,290	1,256	1,322	1,355	1,403	1,450	1,500	1,555	3.3%

Brand Contribution / Yr. to Sep	2009	2010	2011	2012	2013	2014E	2015E	2016E	2017E	2018E	5yr CAGR
GB Stills	157	169	150	141	155	160	167	173	178	184	3.6%
GB Carbs	151	184	189	189	200	210	219	227	235	244	4.0%
International	8	9	11	8	14	16	17	20	23	26	13.0%
Ireland	71	64	58	45	49	50	52	54	55	57	3.0%
France	-	24	62	59	68	69	72	74	77	80	3.3%
Total Brand Contribution	386	450	470	442	486	505	526	549	569	591	4.0%

Brand Contribution Margins / Yr. to Sep	2009	2010	2011	2012	2013	2014E	2015E	2016E	2017E	2018E	5-yr chg
GB Stills	44.7%	46.6%	42.7%	43.9%	45.4%	46.1%	46.4%	46.8%	46.8%	46.9%	1.4%
GB Carbs	36.3%	39.2%	37.6%	36.4%	37.3%	37.9%	38.2%	38.5%	38.5%	38.6%	1.3%
International	33.9%	34.9%	37.5%	28.3%	37.6%	35.6%	33.6%	34.6%	35.1%	35.6%	-2.0%
Ireland	37.4%	35.8%	35.5%	32.2%	35.8%	36.7%	37.4%	38.1%	38.2%	38.2%	2.5%
France		28.3%	25.3%	23.8%	25.1%	25.2%	25.5%	25.6%	25.8%	25.9%	0.9%
Group	39.4%	40.1%	36.4%	35.2%	36.7%	37.3%	37.5%	37.8%	37.9%	38.0%	1.3%

Source: Company Reports and Citi Research Estimates

Figure 33. Consumer Staples – Citi ratings and target prices

	Currency	Share price	Citi Rating	Target
Coca-Cola Hellenic	GBP	1610	Neutral	1700
Beiersdorf	Euro	72.2	Buy	85
Britvic	GBP	672	Buy	850
Carlsberg	DKK	572	Neutral	600
ABI	Euro	72.6	Buy	87
AB Foods	GBP	2244	Neutral	2350
Heineken	Euro	46.6	Neutral	56
SABMiller	GBP	2981	Neutral	3200
Diageo	GBP	1883	Buy	2320
Henkel	Euro	79.2	Neutral	83
Pernod	Euro	79.5	Neutral	91
Danone	Euro	51.1	Neutral	56
Remy	Euro	59.7	Sell	59
BAT	GBP	3124	Buy	3800
Unilever	Euro	27.9	Neutral	30
Nestle	CHF	63.1	Buy	72
L'Oreal	Euro	124	Neutral	125
Tate & Lyle	GBP	772.5	Buy	900
Reckitt Benckiser	GBP	4576	Buy	5400
Swedish Match	SEK	195	Neutral	225
C&C	Euro	4.49	Neutral	
Imperial Tobacco	GBP	2236	Neutral	2500

Source: Reuters prices 13/12/13, Citi Research

Britvic

Company description

Britvic is the No2 soft drinks company in Great Britain. It has a range of own brands, including Robinsons, Fruit Shoot and J2O. The company is also a key bottler for PepsiCo in the UK and Ireland and in May 2010, Britvic entered the French syrups and juice market, with the Fruité acquisition. More recently Britvic has established a number of "reverse" franchise agreements for the distribution of the Fruit Shoot brand in the US, Australia and Spain.

Investment strategy

We have a Buy rating. We think Britvic can deliver about 13% EPS CAGR over FY13-16E, which is almost best in class in our European staples coverage universe, and we believe there is a good chance of upgrades, particularly from three sources: (1) Fruit Shoot intl, (2) further cost savings and (3) improving UK macro. In total we believe the upside to our EPS forecasts could be 9-39% on a 4-5 year view, depending on the scenarios.

Valuation

Our price target is 850p. This is what we believe to be the 12-month fair value resulting from a probability-weighted scenario analysis based on CY17 PEs. We currently forecast CY17 EPS of 57p, but we believe there could be material upside to this, primarily from Britvic’s international expansion. Depending on how much of this upside comes through, we think CY17 EPS could be between 57p and 78p. Under four different scenarios, we value the stock between 613-1,097p. Our 850p target assigns a 25% probability to each of these 4 different scenarios

Risks

Factors which could prevent the achievement of our target price for Britvic include: (1) loss of the Pepsi franchise; (2) increased competition in carbonates market from CCE; (3) limited success in international expansion; (4) failure to deliver cost savings; (4) material commodity and/or concentrate price increases that could affect profitability if Britvic were unable to pass on the increases; (5) implementation of a tax on soft drinks in the UK or Ireland. Factors which could enable the share price to exceed our target price include improving sales momentum in its core markets and evidence that Britvic's recent international franchise agreements are delivering strong sales growth and can make a difference to the company's P&L in the medium term.

Appendix A-1

Analyst Certification

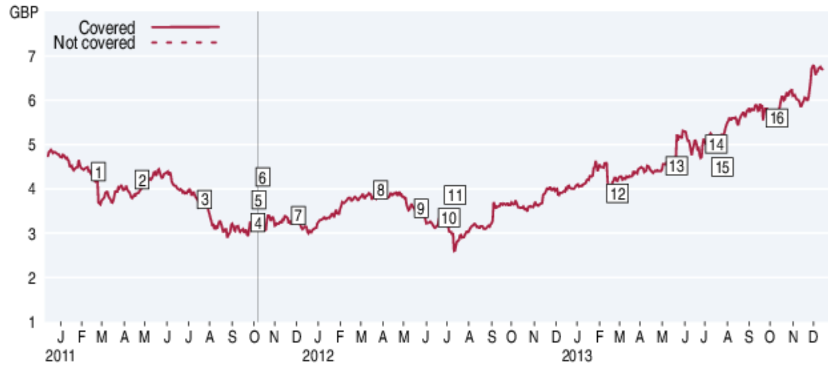
The research analyst(s) primarily responsible for the preparation and content of this research report are named in bold text in the author block at the front of the product except for those sections where an analyst's name appears in bold alongside content which is attributable to that analyst. Each of these analyst(s) certify, with respect to the section(s) of the report for which they are responsible, that the views expressed therein accurately reflect their personal views about each issuer and security referenced and were prepared in an independent manner, including with respect to Citigroup Global Markets Inc and its affiliates. No part of the research analyst's compensation was, is, or will be, directly or indirectly, related to the specific recommendation(s) or view(s) expressed by that research analyst in this report.

IMPORTANT DISCLOSURES

Britvic (BVIC.L)

Ratings and Target Price History
Fundamental Research

Analyst: Andrea Pistacchi



	Date	Rating	Target Price	Closing Price
1	24-Feb-11	1M	*5.30	3.69
2	27-Apr-11	1M	*5.00	4.03
3	25-Jul-11	1M	*4.60	3.66
4	7-Oct-11	Stock rating system changed		
5	8-Oct-11	*1	4.60	3.18
6	14-Oct-11	1	*3.90	3.17
7	5-Dec-11	1	*3.80	3.32
8	29-Mar-12	1	*4.35	3.82
9	25-May-12	1	*4.10	3.46
10	4-Jul-12	1	*3.90	3.04
11	12-Jul-12	1	*3.30	2.61
12	27-Feb-13	1	*4.75	4.18
13	22-May-13	1	*5.60	5.23
14	17-Jul-13	1	*5.80	5.08
15	25-Jul-13	1	*5.90	5.22
16	10-Oct-13	1	*6.40	5.70

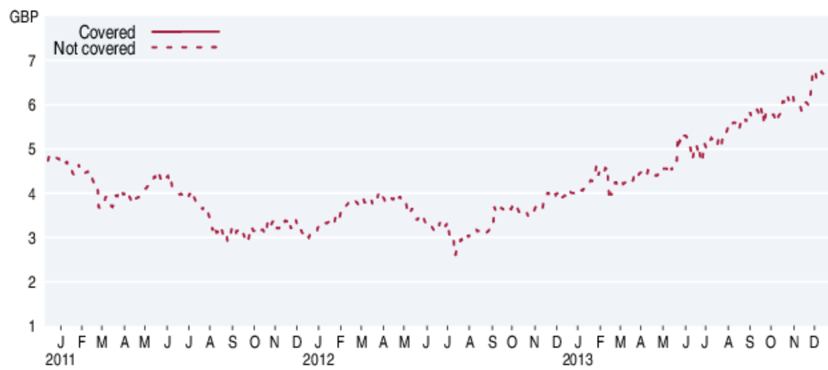
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Britvic (BVIC.L)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Andrea Pistacchi



* Indicates change

Rating/target price changes above reflect Eastern Standard Time

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Data current as of 30 Sep 2013	Buy	Hold	Sell	Buy	Hold	Sell
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